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PROTECTING OLDER AMERICANS AGAINST OVERPAYMENT OF INCOME TAXES

(Deductions You Are Entitled
To Use for 1990)

AN INFORMATION PAPER

PREPARED FOR USE BY THE

SPECIAL COMMITTEE ON AGING
UNITED STATES SENATE

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PREFACE

To help assure that older Americans claim every legitimate income tax deduction, exemption, and tax credit, the Senate Special Committee on Aging, in cooperation with the Internal Revenue Service, has prepared this information paper for tax year 1990. We hope this knowledge helps you in filling out your tax forms.

Keeping up with new tax provisions and filling out tax forms can be a very complicated process. In providing this information paper, the Senate Special Committee on Aging hopes to be of assistance to you.

DAVID PRYOR,
Chairman.
JOHN HEINZ,
Ranking Minority Member.

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ASSISTANCE AVAILABLE TO YOU

Publications to assist you. The Internal Revenue Service prepares many free publications to help answer your tax questions. In addition to the general Publication 17, "Your Federal Income Tax," publications are available on specific topics, such as:

PUBLICATION NUMBERS AND TITLES

1 Your Rights as a Taxpayer.
17 Your Federal Income Tax.
505 Tax Withholding and Estimated Tax.
524 Credit for the Elderly or the Disabled.
530 Tax Information for Homeowners.
553 Highlights of 1990 Tax Changes.
554 Tax Information for Older Americans.
575 Pension and Annuity Income (Including Simplified General Rule).
721 Comprehensive Tax Guide to U.S. Civil Service Retirement Benefits.
907 Tax Information for Persons with Handicaps or Disabilities.
910 Guide to Free Tax Services.
915 Social Security Benefits and Equivalent Railroad Retirement Benefits.

Single copies of any IRS publication can be ordered by mail, using the order form in your tax package or by calling IRS toll-free at 1-800-829-3676. They also may be found at public libraries, post offices, and some banks.

Other special IRS programs offering free assistance.—Through the tax counseling for the elderly (TCE) program, IRS-trained volunteers assist individuals age 60 or older with their tax returns at neighborhood locations in many areas. In addition, certain volunteer income tax assistance (VITA) aides have been trained to help older Americans with their tax returns. (VITA as-

sistance is also available to persons who cannot afford professional tax help as well as to military, handicapped, and non-English-speaking individuals.) To find the location nearest to you, call the IRS toll-free number, 1-800-829-1040.

Private Tax Return Preparers.—You are responsible for the accuracy of every item entered on your return. If you pay someone to prepare the return for you and there is a mistake, the IRS will ask you, and not the preparer, to pay any back taxes, interest, and/or penalties. Therefore, you should be careful to choose someone who understands tax matters and who will prepare a complete and accurate return.

The law requires a paid preparer to sign the return and to complete the Paid Preparers Use *Only* section at the bottom of the form, just below your signature. You should also know how to locate this person in the future if the IRS has a question about your return.

FILING STATUS

In general, your filing status depends on whether you are considered single or married on the last day of your tax year. If you file a calendar year return, your last day generally is December 31. Each filing status has a different tax rate. If more than one filing status applies to you, choose the one that gives you the lowest tax. There are five filing statuses.

Single.—Generally, you are single if you were never married or you were divorced as of December 31, 1990. You are also considered single if you were legally separated, according to your State law, under a decree of divorce or a decree of separate maintenance.

Married Filing a Joint Return.—Generally, you are married if you were legally married as of December 31, 1990, even if you did not live with your spouse in 1990. You are also considered married if your spouse died in 1990 and you did not remarry in 1990. You may file a joint return even if only one spouse had all the income. However, **both** spouses must sign the tax return and **both** spouses are jointly and separately responsible for paying the tax.

Married Filing a Separate Return.—Most married couples pay less tax by filing a joint tax return. However, you can choose to file separate tax returns. After the

due date of the return, you may not choose to file separate returns if you first filed a joint return for that year.

Head of Household.—If you were unmarried or considered unmarried as of December 31, 1990, and you provide more than half the cost of keeping up a home (that was the main home) for yourself and your unmarried child (regardless of his/her age or whether he/she was financially dependent on you) for more than 6 months, you may be eligible to file as head of household. You may also be able to file as head of household if you are entitled to claim other relatives such as your mother or father, or your married child as dependents.

Qualifying Widow(er) with dependent child.—If your spouse died in 1988 or 1989 and you remained unmarried in 1990, you may be able to continue to pay taxes at the lower joint tax rates if: (1) your dependent child lived with you for the entire year, except for temporary absences; (2) you paid more than one-half of the costs of keeping up your home during all of 1990; and (3) you were entitled to file a joint return with your spouse for the year your spouse died. If you do not qualify because your spouse died before 1988 you may still be able to file as head of household.

WHO MUST FILE—BY FILING STATUS AND GROSS INCOME*

You must file a return for 1990 even though you owe no tax if:	*And your gross income was at least:*
1. You were single and were:	
Under age 65	$5,300
Age 65 or older	$6,100
2. You were married filing a joint return and were living with your spouse at the end of 1990 or on the date your spouse died and:	
Both were under age 65	$9,550
One spouse was age 65 or older	$10,200
Both spouses were age 65 or older	$10,850
3. You were married filing a separate return or married but not living with your spouse at the end of 1990 or on the date your spouse died (regardless of age)	$2,050
4. You were unmarried or considered unmarried as of December 31, 1990, and you provided over half the cost of keeping up a home (the main home) for yourself and a dependent (See Head of Household earlier), and were:	
Under age 65	$6,800
Age 65 or older	$7,600
5. You were a qualifying widow or widower with a dependent child and:	
Under age 65	$7,500
Age 65 or older	$8,150
6. You received *any* advance earned income credit (EIC) payments from your employer(s) during 1990.	

* Being blind does not change your filing requirement.

7. You were self-employed and your net earnings from this work were at least $400, then you must file a return to pay self-employment tax. This rule applies regardless of your age, whether or not you are receiving Social Security benefits, and even if you do not otherwise have to file a Federal tax return. You are self-employed if you carry on a trade or business as a sole proprietor, a member of a partnership, or an independent contractor. This includes certain part-time work that you do at home or in addition to your regular job.
8. If you work for a church or a qualified church-controlled organization that elected exemption from Social Security taxes, you will have to pay self-employment tax if you are paid $100 or more in a year by the church or organization.
9. You can be claimed as a dependent on another taxpayer's return. As a dependent, you must file an income tax return if you are:

   (1) Single and—
   - Your earned income was more than $3,250 ($4,050 if 65 or older or blind); or
   - Your unearned income was more than $500 ($1,300 if 65 or older or blind; $2,100 if both 65 or older AND blind); or
   - Your gross income was more than the total of your earned income (up to $3,250) or $500, whichever is larger; plus $800 if 65 or older or blind ($1,600 if both 65 or older AND blind).

   (2) Married and—
   - Your gross income was at least $5 and your spouse files a separate return and itemizes deductions; or
   - Your earned income was more than $2,725 ($3,375 if 65 or older or blind); or
   - You have unearned income and your gross income was more than $500 ($1,150 if 65 or older or blind; $1,800 if both 65 or older AND blind); or

- Your gross income was more than the total of your earned income (up to $2,725), or $500, whichever is larger; plus $650 if 65 or older or blind ($1,300 if both 65 or older AND blind).

10. You owe any tax on an IRA or a qualified retirement plan. See "Individual Retirement Arrangements Distributions," later.

You should file a return for 1990, even though you owe no tax if:

1. Income tax was withheld from your pay. You can get a refund of the tax withheld, even if you are not required to file a return.
2. You qualify for the earned income credit.

FILING DEADLINE

For 1990 income tax returns, the filing deadline is midnight, Monday, April 15, 1991. Any return postmarked after April 15 may be subject to tax penalties unless an individual request for an extension of the deadline is filed by that date. All taxes, however, must be paid by April 15 even if you request an extension of time to file your return.

INCOME TAX FORMS

There are three forms for filing Federal income tax returns:

- Form 1040EZ,
- Form 1040A, and
- Form 1040.

If you filed tax returns in the past, a tax package which includes instructions should be mailed to you by early January. If you do not receive the correct tax return package, you can generally find the forms you need at any participating local library, post office, or bank. You can also call the IRS toll-free forms number, 1-800-829-3676, to request forms or publications.

Form 1040EZ.—Form 1040EZ is the simplest tax return and is used only by *single individuals* who are under age 65 and not blind. You cannot claim any dependents, any adjustments to income, any itemized deductions, or any tax credits on Form 1040EZ. All your income must come from wages, salaries, tips, taxable scholarships and fellowships, and taxable interest of

$400 or less. Your total income must be less than $50,000.

However, most older Americans should use either Form 1040A or Form 1040.

Form 1040A.—Form 1040A has been extensively revised for 1990. Many older Americans who filed Form 1040 last year may be able to file Form 1040A instead this year. Form 1040A can be used for any filing status (explained earlier). Your total income must be less than $50,000. In 1990, lines were added for payments received from Individual Retirement Arrangements (IRAs), pension and annuity payments, and taxable Social Security or equivalent Railroad Retirement benefits. Other income which can be reported on Form 1040A includes wages, salaries, tips, taxable scholarships and fellowships, interest, dividends, and unemployment. If you have any other type of income such as self-employment income or capital gains, you must use Form 1040. The only adjustment to income that you can take on Form 1040A is the deduction for certain contributions to an IRA. (Nondeductible IRA contributions can be reported by attaching Form 8606, *Nondeductible IRA Contributions, IRA Basis, and Nontaxable Distribution(s),* to Form 1040A.) In addition to the earned income credit, the revision contains two new credit schedules: Schedule 2 for the Child and Dependent Care Expenses and Schedule 3 for the Credit for the Elderly or the Disabled. You can use Form 1040A even if estimated tax payments were made for 1990 or you take the new exclusion of Series EE savings bond (issued after 1989) interest for qualified higher education expenses.

Form 1040.—Form 1040 is used by all other individuals except nonresident aliens. Form 1040 must be used if your total taxable income is $50,000 or more, or you itemize your deductions such as home mortgage interest, medical and dental expenses, job expenses, etc. Capital gains or losses can be reported only on Form 1040. If you owe self-employment taxes or alternative minimum tax, you must use Form 1040.

PRESIDENTIAL ELECTION CAMPAIGN FUND

You may voluntarily choose to have $1 of your taxes ($2 on a joint return) paid into this fund to help pay for Presidential election costs. Making this choice will not

change the amount of tax you pay or the amount of refund you will receive.

EXEMPTIONS AND DEPENDENTS

You are allowed a $2,050 deduction for each exemption shown on your tax return (line 6e, Form 1040A or Form 1040). You can claim yourself, your spouse, your minor children, or any other relative or member of your household if all five dependency tests (listed below) are met for that individual. However, you may not take an additional exemption if you are age 65 or older or blind. Instead, you are allowed a higher standard deduction amount if you qualify. See the discussion on standard deduction.

The Dependency Tests

There are five tests to determine whether someone is your dependent: relationship, married person, citizen or resident, income, and support tests. Each dependent must meet all five of the following tests.

Test 1: Relationship.—Your dependent must be either your relative or someone who lived in your home as a member of your household all year. Any relationships established by marriage are not treated as ended by divorce or death. The relationship must not violate local law.

The following are considered your *relatives:*

- Your child. Your child includes your son, daughter, stepchild, adopted child; a child who lived in your home as a family member if placed with you by an authorized placement agency for legal adoption; and a foster child (any child who lived in your home as a family member for the whole year).
- Your grandchild, great-grandchild, etc.
- Your son-in-law, daughter-in-law.
- Your parent, grandparent, stepparent, parent-in-law.
- Your brother, sister, stepbrother, stepsister, brother-in-law, sister-in-law, half brother, half sister.
- If related by blood, your aunt, uncle, nephew, niece.

Test 2: Married person.—Your married dependent cannot file a joint return. However, if neither the dependent nor the dependent's spouse is required to file, but they file a joint return to get a refund of all tax

withheld, you may claim him or her if the other four tests are met.

Test 3: Citizen or resident.—The dependent must be either a U.S. citizen or resident alien or a resident of Canada or Mexico or your adopted child who is not a U.S. citizen but who lived with you all year in a foreign country.

Test 4: Income.—Generally, the dependent's gross income must be less than $2,050. Gross income does not include nontaxable income, such as welfare benefits or nontaxable Social Security benefits.

If, in 1990, your dependent was permanently and totally disabled and had income from services performed at a sheltered workshop school, that income is generally not included for purposes of the income test. For details, get Publication 501, *Exemptions, Standard Deduction, and Filing Information.*

Special rules for your dependent child: Your dependent who is your child does not have to meet this income test if either your child was under 19 at the end of 1990, or your child qualifies as a student dependent and was under age 24 at the end of 1990.

Your child is a "student dependent" if he or she:

- Was enrolled as a full-time student at a school during any five months in 1990, or
- Took a full-time, on-farm training course during any five months of 1990. (The course had to be given by a school or a State, county, or local government agency.)

To be a full-time student, the child must be enrolled in school for the number of hours or classes that the school considers to be full-time.

The school must have a regular teaching staff, a regular course of study, and a regularly enrolled body of students in attendance. School includes elementary, junior, and senior high schools; colleges, universities; and technical, trade, and mechanical schools. It does not include on-the-job training courses or correspondence schools.

Test 5: Support.—The general rule is that you had to provide over half the dependent's support in 1990. If you file a joint return, support can come from either spouse. For exceptions to the support test, see the instructions for Form 1040.

Support includes food, a place to live, clothing, medical and dental care, and education. Support also in-

cludes such items as a car and furniture, but only if they are given to the dependent, or if the dependent buys them, solely for his or her own use or benefit. In figuring support, use the actual cost of these items. However, you should figure the cost of a place to live at its fair rental value. In figuring support, you must include money used by the dependent for his or her own support, even if this money was not taxable. Examples are Social Security and welfare benefits, gifts, and savings.

Support does not include such items as income and Social Security taxes, life insurance premiums, or funeral expenses.

Multiple Support Agreements

The support test is met if the person claiming the exemption contributed more than one-half of the individual's total support during the calendar year. But in some cases, two or more individuals provide support for an individual, and no one individual has contributed more than half the person's support. However, it still may be possible for one of the individuals to claim the $2,050 exemption if all of the following requirements are met:

(1) Two or more persons—any one of whom could claim the person as a dependent if it were not for the support test—together contribute more than half of the dependent's support.

(2) Any one of those who individually contributes more than 10 percent of the mutual dependent's support, but only one of them may claim an exemption for the dependent.

(3) Each of the others who individually contributes more than 10 percent must sign a written statement that he or she will not claim the dependency exemption for that year. The statement must be filed with the income tax return of the person who claims the dependency exemption. Form 2120, "Multiple Support Declaration," is used for this purpose.

Note. You can include with your medical expenses those medical expenses you paid for a person for whom you meet the support test under a multiple support agreement, even if you may not claim the person as a

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dependent because he or she had gross income of $2,050 or more.

INCOME

Generally, you must include in gross income everything you receive in payment for personal services. In addition to wages, salaries, commissions, tips and fees, this includes other forms of compensation such as fringe benefits and payments for certain expenses you incur. You must report income in the form of goods or services at the fair market value of the goods or services you received. Income of particular interest to older Americans includes certain nontaxable income, interest, dividends, gain from the sale of a main home, pensions and annuities, distributions from IRAs, Social Security and equivalent Railroad Retirement benefits, and gambling and lottery winnings.

Nontaxable Income

Generally gifts and inheritances you receive are not taxable to you; the person making the gift/bequest already paid taxes, if any, on the income used to purchase the gift or to build the estate. However, if you later receive income such as interest, dividends, or rents from such property, that income is taxable to you. Department of Veterans Affairs payments and/or insurance proceeds paid at the death of the insured are usually tax free.

Dividends and Interest

Dividend and interest income is generally taxable. However, interest earned on notes or bonds issued by a State or local government may not be taxable. You must show on your tax return any tax-exempt interest you received or accrued during the tax year. This is an information-reporting requirement and does not convert tax-exempt interest to taxable interest. You must report the entire amount of your ordinary dividends as taxable income. If you fail to provide the payer of interest and dividends with your correct Social Security number or you do not include all of this income on your return, the IRS can require the payer to withhold 20 percent of future interest and dividend income as payment for taxes due.

Interest Exclusion for Qualified U.S. Savings Bonds

Beginning in 1990, all or part of the interest from certain U.S. savings bonds can be excluded from income if you pay qualified higher education expenses during the year you redeem the bonds. The bonds must have been issued after 1989 to an individual age 24 or older. Qualified higher education expenses are tuition and required fees at a college or eligible vocational school for the bonds' owner or the owner's spouse or dependent. For more information, see Publication 550, "Investment Income and Expenses."

Sale of Your Main Home

If you sold your main home during the year, you must report the sale or exchange of your home on Form 2119, "Sale of Your Home." You may be able either to postpone paying tax on some or all of the gain or to exclude the gain from your taxable income. In either case, you must use Form 2119 to inform IRS that you meet certain qualifications. If you are unable to either postpone the tax on the gain or to exclude the gain from gross income, then the taxable gain for the sale is reported on Schedule D, "Capital Gains and Losses." You cannot deduct a loss on the sale of your home. The loss has no effect on the basis of your new home.

• *Postponement of Gain.*—If, within 2 years before or 2 years after the date of sale, you purchase (or build) and live in another main home that costs at least as much as the adjusted sale price of the old home, your entire gain on the sale is postponed at the time of the sale or exchange. You need not use the same funds received for the sale of your old home to buy or build your new home. The tax on the gain is postponed, not forgiven. Any gain not taxed in the year of sale is subtracted from the cost of your new home, giving you a lower basis in the new home.

• *Exclusion of Gain.*—Special rules apply to the sale of a main home by persons age 55 or older. If (1) you were age 55 or older on the date of the sale or exchange of your main home, (2) you owned and lived in the home for at least 3 years of the 5-year period ending on the date of the sale or exchange, and (3) you or your spouse (depending on your marital status on the date of the sale) have never excluded gain on the sale or exchange

of a home after July 26, 1978; then, you may elect to exclude up to $125,000 ($62,500 if you are married filing separately) of the gain from gross income whether or not you purchase a new home.

In the case of a jointly owned home, both you and your spouse will meet the age, ownership, and use tests if:

- You hold the home either as joint tenants, tenants by the entirety, or as community property on the date of the sale or exchange;
- You file a joint return for the tax year in which you sell the home; and
- Either of you are 55 or older on the date of the sale and has owned and lived in the property as a main home for the required time before the sale or exchange.

If the home is not jointly owned, the spouse who owns the property must meet the age, ownership, and use tests. The other spouse must join in making the choice.

If you become physically or mentally unable to care for yourself and live in a nursing home or a State-licensed facility, you will be considered to have lived in your home as your main home during your stay in the facility if you have owned and lived in your home as your main home for a total of at least 1 year during the 5-year period. This exception applies to sales after September 30, 1988.

For more complete information, get Publication 523, "Tax Information on Selling Your Home."

Pensions and Annuities

You should receive a Form W-2P or Form 1099-R showing the amount of your pension or annuity. Be sure to attach Form W-2P to your return. Your pension or annuity payments are fully taxable if you did not contribute to the cost of your pension or annuity, or you used the 3-Year Rule and you got back tax-free your entire cost before 1990. Fully taxable pensions and annuities also include military retirement pay shown on Form W-2P and any taxable Railroad Retirement benefits shown in Box 12 of Form RRB-W-2P.

If your pension or annuity is not fully taxable and your Form W-2P does not show the taxable part, you must use the General Rule to figure the taxable part.

The General Rule is explained in Publication 939, *Pension General Rule (Nonsimplified Method).* But, if your annuity starting date was after July 1, 1986, you may be able to use the Simplified General Rule as explained in Publication 575, *Pension and Annuity Income (Including Simplified General Rule).* If your pension is civil service, you should get Publication 721, *Comprehensive Tax Guide to U.S. Civil Service Retirement Benefits.*

If you receive a lump-sum payment, you may be eligible to lower the taxes due on it by using Form 4972, *Tax on Lump-Sum Distributions.* For details, get Form 4972.

Individual Retirement Arrangements (IRAs) Distributions

Distributions from an IRA, whether from principal or earnings, are generally fully taxable when received. Exceptions to this general rule include rollovers and timely withdrawals of excess contributions. See Publication 590, *Individual Retirement Arrangements (IRA's),* for more information on rollovers and excess contribution withdrawals. If you have made nondeductible contributions to your IRA, you have a cost basis in your IRA. The part of any distributions representing a return of your nondeductible contributions is not taxed when distributed to you. A 10-percent tax in addition to the regular income tax applies to any distributions before age 59½ except in certain cases such as the death or disability of the IRA owner. Distributions must begin by April 1 of the calendar year following the year in which you become age 70½ to avoid substantial additional taxes.

SOCIAL SECURITY AND RAILROAD RETIREMENT TAXABILITY

Generally, you will owe taxes on some (but never more than half) of your Social Security and equivalent Railroad Retirement benefits if your total income minus half of your benefits exceeds $25,000 for single and married persons who live apart all year and do not file a joint return or $32,000 for married couples who file a joint return. Married couples who live together but file separate tax returns must include part of their benefits

in taxable income regardless of the amount of their total income.

• *Social Security.*—You should receive Form SSA–1099, "Social Security Benefit Statement," if you received benefits in 1990. This form will show any deductions made by Social Security from your total benefits, such as Medicare premiums, repayments of prior-year overpayments, etc. If you do not receive an SSA–1099 by early February or you believe the statement to be incorrect, you should call the SSA toll-free number, 1–800–234–5772.

To estimate whether you must include any of your Social Security benefits in taxable income, add up your income from *all* sources including any tax-exempt interest you may have received and one-half of your net benefits (Box 5 of your SSA–1099).

• If your total income is $25,000 or less and you are a single person or a married person filing separately and did not live with your spouse at any time during the year ($32,000 for married couples filing a joint return), then none of your benefits will be included.

• If your total income exceeds $25,000 and you are a single person or a married person filing separately and did not live with your spouse at any time during the year ($32,000 for married couples filing a joint return), then some of your benefits will be included. You will need to figure the taxable part of your benefits by using the worksheet on page 16 of the Form 1040 Instructions.

• If your total income exceeds $0 and you are a married person who lives together with your spouse during the year and files a separate tax return, then some of your benefits will be includable in taxable income. For more information, get Publication 915, "Social Security Benefits and Equivalent Railroad Retirement Benefits."

• *Railroad Retirement Benefits.*—A Railroad Retirement benefit is comprised of up to four different parts. Before 1984, only the supplemental annuity was taxable. Beginning in 1984, the other three parts became taxable but each in a different way. Only the Social Security equivalent portion of tier I benefits is taxed in the same manner as Social Security benefits. Tier II and the non-Social Security equivalent portion of tier I benefits are fully taxable after they exceed your contributions which were deducted during your career. Vested dual benefits are also fully taxable.

The Railroad Retirement Board will send each beneficiary a Form RRB-1099 showing the equivalent tier I benefits paid. The Form RRB-W-2P covers the other three parts. If you receive both Social Security benefits and Railroad Retirement benefits, you should use the Railroad Retirement worksheet. More complete information can be found in Publication 575, *Pension and Annuity Income (Including Simplified General Rule).*

ADJUSTMENTS TO INCOME

Once you have figured your total income, you may "adjust" it downward with any of six major adjustments to arrive at adjusted gross income. The only adjustment to income that can be taken on Form 1040A is the deduction for contributions to an IRA. All other adjustments must be taken on Form 1040. You do not have to itemize to take these adjustments to income. Employee business expenses are no longer an adjustment to income (but they are an itemized deduction on Schedule A) except for certain performing artists and handicapped employees.

Individual Retirement Arrangements.—An IRA is a personal savings plan that lets you set aside money for your retirement. You may be able to deduct contributions you make to an IRA in whole, or in part, depending on your circumstances. Earnings and gains on your IRA generally are not taxed until they are distributed to you. Generally, you can contribute up to the lesser of your taxable compensation, or $2,000. If you (or your spouse) were covered at any time during the year by an employer's retirement plan, your deduction may be limited. If your deduction is limited, you can still make nondeductible contributions up to the remaining amount of your contribution limit. If you file a joint return with your spouse (who did not work during the year), you may be eligible to contribute up to $2,250 into two separate IRAs (one for you and one for your spouse, a spousal IRA). You can divide the contribution between the two accounts in any way except that neither account can be credited with more than $2,000. See Publication 590, *Individual Retirement Arrangements (IRAs),* for more information.

If you were age 70½ or older by the end of 1990, you cannot deduct any contributions made to your IRA or treat them as nondeductible contributions.

Keogh plans.—You must have net earnings from self-employment to claim a deduction for payments to a Keogh (H.R. 10) plan. For information on Keogh plans, see Publication 560, "Retirement Plans for the Self-Employed."

One-Half of Self-Employment Tax.—Beginning in 1990, if you had income from self-employment and you owe self-employment tax, you may deduct one-half of that tax. But you will first need to complete Schedule SE to figure your deduction.

Then enter on line 25 one-half of the self-employment tax shown on line 10 of Schedule SE, Section A or Section B, whichever applies.

Self-Employed Health Insurance Deduction.—If you were self-employed and had a net profit for the year, or, if you received wages in 1990 from an S corporation in which you were a more than 2 percent shareholder, you may be able to deduct part of the amount paid for health insurance on behalf of yourself, your spouse, and dependents. But you may not take the deduction if you were eligible to participate in any subsidized health plan maintained by your employer or your spouse's employer. For more details, get Publication 535, *Business Expenses.*

Other Adjustments to Income.—In addition, you may be eligible to take certain other adjustments to income. They include penalty on early withdrawal of savings, alimony paid, and jury duty pay given to your employers. For details, see Form 1040 instructions.

STANDARD DEDUCTION

The standard deduction reduces your taxable income. It also reduces the need for many taxpayers to itemize their deductions. The standard deduction, which depends on your filing status (explained earlier) and whether you are age 65 or older or blind, is not built into the Tax Table or Tax Rate Schedules but is figured separately. Once you have figured your standard deduction amount, you should then decide which gives you a higher tax benefit—taking the standard deduction or itemizing your deductions on Schedule A of Form 1040.

If you are age 65 or older or blind in 1990 you are entitled to a standard deduction amount which is more than the amount for taxpayers under 65 and not blind. You are considered 65 for the 1990 tax year if your 65th birthday was on or before January 1, 1991. You are considered blind for 1990 if you are blind on the last day of 1990. Your tax instruction booklet has more information on the requirements.

Special rules. Your standard deduction is zero if your spouse itemizes deductions on a separate return, you are a dual-status or nonresident alien, or you have a short tax year. If you can be claimed as a dependent on another person's tax return, your standard deduction may be limited. If you meet one of these special rules, you may not use the standard deduction table which follows. See your tax instruction booklet for more details on these special rules.

Use one of the following charts. Choose the chart that fits your personal situation.

Caution. *If you are married filing a separate return and your spouse itemizes deductions, or if you are a dual-status alien, you* ***cannot*** *take the standard deduction even if you were 65 or older or blind.*

Standard Deduction Chart for Most People

DO NOT use this chart if you were 65 or older or blind, OR if someone can claim you as a dependent.

If your Filing Status is:	Your standard deduction is:
Single	$3,250
Married filing joint return or Qualifying widow(er) with dependent child	$5,450
Married filing separate return	$2,725
Head of household	$4,750

Standard Deduction Chart for People Age 65 or Older or Blind

If someone can claim you as a dependent, use the worksheet below, instead.

If you were 65 or older or blind, check the correct number of boxes below. Then go to the chart.

You	65 or older ☐	Blind ☐
Your spouse, if claiming spouse's exemption	65 or older ☐	Blind ☐

Total number of boxes you checked ☐

If your Filing Status is:	and the number in the box above is:	Your standard deduction is:
Single	1	$4,050
	2	4,850
Married filing joint return or Qualifying widow(er) with dependent child	1	$6,100
	2	6,750
	3	7,400
	4	8,050
Married filing separate return	1	$3,375
	2	4,025
	3	4,675
	4	5,325
Head of household	1	$5,550
	2	6,350

Standard Deduction Worksheet for Dependents

Use this worksheet ONLY if someone can claim you as a dependent (Keep for your records)

If you were 65 or older or blind, check the correct number of boxes below. Then go to the worksheet.

You	65 or older ☐	Blind ☐
Your spouse, if claiming spouse's exemption	65 or older ☐	Blind ☐

Total number of boxes you checked ..... ☐

1. Enter your **earned income** (if none, enter 0)	1.	
2. Minimum amount	2.	$500
3. Compare the amounts on lines 1 and 2. Enter the **larger** of the two amounts	3.	
4. Enter the amount shown below for your filing status. • Single, enter $3,250 • Married filing separate return, enter $2,725 • Married filing jointly or Qualifying widow(er) with dependent child, enter $5,450 • Head of household, enter $4,750	4.	
5. **Standard deduction.**		
a. Compare the amounts on lines 3 and 4. Enter the **smaller** of the two amounts. If under 65 and not blind, stop here. This amount is your standard deduction. Otherwise, go on to line 5b	5a.	
b. If 65 or older or blind, multiply $800 ($650 if married filing a joint or separate return, or qualifying widow(er) with dependent child) by the total number of boxes you checked above. Enter the result	5b.	
c. Add lines 5a and 5b. Enter the total. This is your standard deduction.	5c.	

CHECKLIST OF ITEMIZED DEDUCTIONS FOR SCHEDULE A (FORM 1040)

Medical and Dental Expenses

Medical and dental expenses are payments you make for the diagnosis, treatment, or prevention of disease. They also include payments for treatment affecting any part or function of the body. Expenses for transportation to get medical care are included in medical expenses. Payments for insurance that provides medical care for you, your spouse, and dependents are included in medical expenses. Unreimbursed expenses are deductible to the extent they are more than 7.5 percent of your adjusted gross income (line 31, Form 1040). Expenses may be deducted only in the year you paid them. If you charge medical expenses on your credit card, deduct the expenses in the year the charge is made regardless of when the bill is paid.

Drugs and medicines.—Amounts paid for medicines and drugs that required a prescription, and for insulin are deductible. These items are included in medical expenses, subject to the 7.5-percent rule.

Expenses for the following are included in your medical and dental expenses:

—Doctors, surgeons, dentists, eye doctors, gynecologists, chiropractors, osteopaths, podiatrists, chiropodists, psychiatrists, psychologists, physical therapists, acupuncturists, Christian Science practitioners, and psychoanalysts.

—Medical examinations, X-rays and laboratory services, surgery, and dental fees.

—Nursing help. However, if you pay someone to do both nursing and housework, you may deduct only the cost of the nursing help.

—Hospital care (including meals and lodging), clinic costs, lab fees.

—Medical treatment (including meals and lodging) at a center for drug addicts or alcoholics.

—Medical aids such as hearing aids (and batteries), false teeth, eyeglasses, contact lenses, braces, artificial limbs, crutches, wheelchairs, guide dogs and the cost of maintaining these aids.

—Oxygen equipment and oxygen to relieve problems in breathing caused by a medical condition.

—Ambulance service and other travel costs to get medical care. If you used your own car, you may claim what you spent for gas and oil to go to and from the place you received medical care, or you may claim 9 cents a mile. Add parking fees and tolls to the amount you claim under either method.
—Cosmetic surgery.
—Cost and repair of special telephone equipment for the deaf.
—Extra cost of a specially equipped television set and the cost of an adapter for a regular set that provides subtitles for a deaf person.
—Part of the cost of braille books and magazines that is more than the price for regular books and magazines.
—Capital expenditures for medical purposes, such as air-conditioning or elevators. If these expenses are for permanent improvements that increase the value of the property, you may include them as medical expenses only to the extent that they cost more than the increase in the value of the property.
—Cost of a nursing home (including meals and lodging) if the principal reason for being in the nursing home is to get medical care.
—Medical care included in the "life-care fee" or "founders fees" of a retirement home that is paid monthly or as a lump sum under an agreement with the home. The deductible part of the fee payment is the amount set apart for medical care.
—Cost of special equipment, such as a motorized wheelchair or autoette, special hand controls and other special equipment installed in a car specifically for the use of a physically handicapped person.

You may only deduct those medical expenses that are more than 7.5 percent of your adjusted gross income.

For more information, see Publication 502, "Medical and Dental Expenses."

Taxes

- Real estate
- Personal property
- State, local, or foreign income

Interest

- Personal loan
- Home mortgage
- Auto loan
- Loans on life insurance
- Installment purchases

For 1990, you may deduct only 10 percent of the interest you paid on loans used for personal purposes, other than qualified home mortgage interest. In most cases, you will be able to deduct all of your home mortgage interest. Whether your home mortgage interest is fully deductible depends on the date you took out the mortgage, the amount of the mortgage, and your use of its proceeds. For more information, see Publication 936, "Limits on Home Mortgage Interest Deduction."

Bank and other general purpose credit cards.—If the credit is used for personal purposes, you may deduct 10 percent of the finance charge added to your monthly statement if no part of the charge was for investigation fees, membership fees, loan fees, service charges, or similar charges.

Points.—When buying a home, "points" may be interest paid in advance or charges for specific services. If the points are charges for specific services they are not deductible. You may deduct the amount you pay as points (provided they are prepaid interest), in the year of payment if the loan is used to buy or improve your main home and is secured by that home. In addition, the payment of points must be an established business practice in the area where the loan was made, the points must not exceed the number of points generally charged in your area, and the points are paid with funds other than those obtained from your lender.

If the home you purchase is not your main home, you may not deduct the full amount of points in the year paid. Instead, the prepaid interest paid as points must be spread over the life of the mortgage, and is deductible over that period.

Points are not deductible if they represent charges for services rendered by the lending institution (e.g., VA or FHA points are not deductible as interest if paid for specific services). Also, points are not deductible if paid by the seller but are selling expenses that reduce the amount realized.

Penalty for prepayment of a mortgage.—This is generally deductible as home mortgage interest if it qualifies. Otherwise, you may deduct it as personal interest.

Revolving charge accounts.—If the account is used for personal purposes, 10 percent of the finance charges may be deducted if they are separately stated on your bill.

Contributions

In general, contributions to qualified organizations, such as those organized and operated for religious, charitable, educational, scientific, or literary purposes may be deducted up to 50 percent of your adjusted gross income (line 31, Form 1040). Contributions "for the use of" any charitable organization or contributions to veterans organizations, fraternal societies, or nonprofit cemetery companies are limited to 30 percent of adjusted gross income (line 31, Form 1040).

If your total contributions for the year are 20 percent or less of your adjusted gross income (line 31, Form 1040), they are fully deductible (provided they otherwise qualify) and it is not necessary to figure whether the limits apply.

To deduct your contributions, you must make them in cash or other property before the close of your tax year. Other property (clothing, books, furniture, etc.) is deducted at the fair market value. You may deduct contributions you charge to your credit card in the year the charge is made.

Examples of other charitable contributions include:

- The cost and upkeep of uniforms that you must wear while performing donated services for a charitable organization.
- Out-of-pocket expenses you pay in giving services to a charitable organization. (Do not deduct the value of your time or services.)
- Payment of more than fair market value to an organization for goods, merchandise, services, banquets, shows, sporting events, etc.
- You may also deduct unreimbursed out-of-pocket expenses directly related to services you give to a charitable organization, such as gas and oil for your car. If you do not want to deduct actual expenses,

you may use a standard rate of 12 cents a mile. In either case you may deduct parking fees and tolls.

Charitable contributions may only be claimed as an itemized deduction on Schedule A (Form 1040). You must keep records to prove your cash and noncash contributions. If your total noncash contributions are over $500, you must attach Form 8283, "Noncash Charitable Contributions," to your return. For more information, see Publication 526, "Charitable Contributions."

Casualty or Theft Losses

You may deduct casualty losses, such as those that result from a tornado, flood, storm, fire, or auto accident (provided it was not caused by a willful act or willful negligence), or theft losses. The amount of your casualty loss deduction is generally the lesser of (1) the decrease in fair market value of the property as a result of the casualty or theft, or (2) your adjusted basis in the property before the casualty or theft. This amount must be reduced by any insurance or other reimbursement you receive.

Your nonbusiness casualty or theft losses are deductible only to the extent that your total losses during the year exceed 10 percent of your adjusted gross income after reducing each separate casualty or theft by $100. You must use Form 4684 to figure your casualty or theft loss. Report your casualty or theft loss on Schedule A (Form 1040).

You may not deduct a casualty or theft loss that is covered by insurance unless you filed a timely insurance claim for reimbursement. However, even if you did not file an insurance claim, you may deduct the part of the loss not covered by insurance. For more information, see Publication 547, "Nonbusiness Disasters, Casualties, and Thefts."

Miscellaneous Deductions

Unreimbursed employee expenses, expenses of producing income, and other qualifying expenses are deducted as miscellaneous itemized deductions on Schedule A (Form 1040). Most miscellaneous itemized deductions are subject to a 2-percent limit. The amount deductible is limited to the total of these miscellaneous deductions that is more than 2 percent of adjusted gross

income. The 2-percent limit is applied after all other deduction limits are considered. Some of the expenses subject to the 2-percent limit are:

- Professional society dues.
- Exployment-related educational expenses.
- Expenses of looking for a new job.
- Professional books, magazines, journals, and periodicals.
- Work clothes and uniforms.
- Union dues and fees.
- 80 percent of unreimbursed business-related meal and entertainment expenses.
- Certain other unreimbursed employee business expenses.
- Safe deposit rental.
- Tax preparation fees.
- Certain investment expenses.

Certain miscellaneous expenses are not subject to the 2-percent limit. These expenses include:

- Federal estate tax on income in respect of a decedent.
- Certain deductions when a taxpayer repays amounts held under a claim of right.
- Amortizable bond premiums on bonds acquired before October 23, 1986.
- Gambling losses to the extent of gambling winnings.
- Unrecovered investment in a pension when the retiree dies before the entire investment is returned.
- Impairment-related work expenses of a handicapped individual that are for deductible attendant care services at the individual's place of work and other expenses in connection with the place of work that are necessary for the individual to be able to work.

For more information, see Publication 529, "Miscellaneous Deductions."

TAX COMPUTATION

You must use the Tax Table to find your tax if your taxable income (line 5, Form 1040EZ; line 22, Form 1040A; or line 37, Form 1040) is less than $50,000. You *must* use this table *unless* your taxable income is $50,000 or more. In that case, you must use the Tax

Rate Schedules. The Tax Table is designed to be used by individuals whether or not they itemize their deductions.

TAX CREDITS

Tax credits are used to reduce the amount of tax you owe. All credits must be taken on Form 1040, with the exception of the Credit for Child and Dependent Care Expenses, the Credit for the Elderly or the Disabled, and the Earned Income Credit which may be taken on Form 1040A. No credits may be taken on Form 1040EZ.

The most common credits are:

Credit for Child and Dependent Care Expenses

A portion of certain payments made for child and dependent care may be claimed as a credit against tax.

If you maintained a household that included your dependent under age 13 *or your disabled dependent, or your disabled spouse,* you may be allowed a tax credit for employment-related child and dependent care expenses. These expenses must have been paid during the tax year in order to enable you (and your spouse if you were married) to work or to look for work. You must have income from work during the year. The maximum amount of child and dependent care expenses that may be used to compute the credit is $2,400 for one qualifying person and $4,800 for two or more qualifying persons.

The credit is 30 percent of your qualifying expenses if your adjusted gross income (line 31 of Form 1040 or line 16 of Form 1040A) is $10,000 or less. The 30-percent rate is reduced by 1 percent for each additional $2,000 (or part of $2,000) of adjusted gross income above $10,000 until the percentage is reduced to 20 percent for adjusted gross income above $28,000.

See the Form 1040A, Schedule 2 instructions or, if you file Form 1040, see Form 2441 for more information, including a special rule for divorced or separated taxpayers.

Also, you must include the name, address, and taxpayer identification number (unless it is an exempt organization) of the care provider on your tax return.

Credit for the Elderly or the Disabled

You may be able to claim this credit if you are: (1) age 65 or over, or (2) under age 65 and retired on a permanent and total disability for which you receive taxable disability benefits in 1990, and under the mandatory retirement age.

Even if you meet one of the above conditions, you generally cannot take the credit if you are:

- Single and the amount of Form 1040, line 32 (Form 1040A, line 16), is $17,500 or more; or you received $5,000 or more of nontaxable Social Security or other nontaxable pensions.
- Married filing a joint return, only one spouse is eligible for the credit, and the amount on Form 1040, line 32 (Form 1040A, line 16), is $20,000 or more; or you received $5,000 or more of nontaxable Social Security or other nontaxable pensions.
- Married filing a joint return, both spouses are eligible for the credit, and the amount on Form 1040, line 32 (Form 1040A, line 16), is $25,000 or more; or you received $7,500 or more of nontaxable Social Security or other nontaxable pensions.
- Married filing a separate return, you did not live with your spouse all year, and the amount on Form 1040, line 32 (Form 1040A, line 16), is $12,500 or more; or you received $3,750 or more of nontaxable Social Security or other nontaxable pensions.

For more information, see Publication 524, Credit for the Elderly or the Disabled.

Earned Income Credit

If you have a child who lives in your main home in the United States for more than half the year with you (for the entire year if the child is a foster child or if your filing status is qualifying widow or widower with dependent child), you may be entitled to a special payment or credit of up to $953. This is called the earned income credit. It may come as a refund check or be applied against any taxes you owe. Generally, if both your earned income and your adjusted gross income were each less than $20,264 in 1990, you may be able to claim the credit.

Earned income means wages, salaries, tips, strike benefits, other employee compensation, certain disability

pensions, nontaxable military quarters and subsistence allowances, and net earnings from self-employment. Your filing status must be married filing jointly, or qualifying widow(er) or head of household. However, certain married persons living apart with a dependent child who qualify for head-of-household status (see Filing Status, earlier) may also be eligible to claim the credit. For more information, see Publication 596, "Earned Income Credit."

REFUND OR AMOUNT YOU OWE

Once you have determined your final tax liability by subtracting out all your credits and adding in any other taxes, you have only one more step—to determine whether you owe the government or the government owes you. If your withholding and estimated tax payments plus any other payments exceed your tax liability, you are due a refund. If not, you should attach a check or money order for the total taxes you owe.

TAX WITHHOLDING AND ESTIMATED TAX PAYMENTS

The Federal income tax system operates on a pay-as-you-go basis. Typically, taxes are withheld from wages, salaries and other forms of compensation including some retirement payments. If taxes are not withheld you are probably required to make quarterly payments to meet your estimated tax liability. Some examples of income from which income tax is not generally withheld are: interest and dividends; self-employment; alimony; rental income; capital gains; and the taxable portion of Social Security benefits.

• *Withholding on pensions and annuities.*—Unless you choose not to have any withheld, Federal income tax will generally be withheld from your taxable pension and annuity payments. This includes distributions from an individual retirement arrangement, from a life insurance company under an endowment, annuity, or life insurance contract, from a pension, annuity, profit-sharing plan or from a stock bonus plan, or from any similar plan that defers the time you receive compensation. The amount withheld depends on whether you receive payments spread out over more than 1 year (peri-

odic payments) or whether you receive all of the payments within 1 year (nonperiodic payments).

Withholding from periodic payments of a pension or annuity is figured in the same way as withholding from salaries and wages. To tell the company that pays your pension or annuity how much you want withheld, fill out Form W–4P, or a similar form provided by the company, showing your marital status and the number of withholding allowances to which you are entitled. If you do not give the payer a Form W–4P, tax will be withheld as if you are married and claiming three withholding allowances. You may also use this form to tell the payer you do not want any tax withheld. However, if you are a U.S. citizen or resident alien whose residence address is in a foreign country, the payer must withhold tax.

Tax will be withheld at the rate of 10 percent on any nonperiodic payments you receive, unless they are part of a "qualified total distribution." A qualified total distribution is payment within 1 year of your entire interest in a pension, profit-sharing, stock bonus, or qualified annuity plan. The amount withheld from a qualified total distribution is specified in tables. The payer can tell you the amount that will be withheld.

Because the withholding rates for nonperiodic payments do not depend on withholding allowances or whether you are married or single, Form W–4P is not used. The withholding rates are fixed. You cannot change the way tax is withheld. However, you can use Form W–4P to choose not to have tax withheld; to revoke a previous choice not to have tax withheld; or to specify that an additional amount be withheld.

• *Estimated tax requirements.*—Remember, if no tax or not enough tax is withheld from your income, you may need to pay estimated tax. Your estimated tax generally is the total of your expected income tax, self-employment tax, and other taxes reported on Form 1040 (or Form 1040A under certain circumstances), less your expected withholding and credits. Form 1040–ES provides a worksheet for making this computation.

If your estimated tax for 1991 is $500 or more and you expect your income tax withholding and credits to be less than the lesser of: (1) 90 percent of the tax liability shown on your 1991 return, or (2) 100 percent of the tax liability shown on your 1990 tax return (assuming

the return covered all 12 months), you generally must pay an estimated tax and use Form 1040-ES. Installment payments are due April 15, June 15, September 15, and January 15, 1992. For more information, see Publication 505, "Tax Withholding and Estimated Tax."

ESTATE AND GIFT TAXES

You generally do not have to pay tax on any cash or property you receive as a gift or inheritance. Likewise, any gift or inheritance you pass on is generally tax-free to the recipient. If you make a gift of more than $10,000 to any one individual in the same year, you—but not the recipient—may be required to pay a gift tax.

For decedents who died during 1986, no Federal estate tax, nor any estate tax return, is due if the value of the decedent's gross estate is $500,000 or less. For decedents who died in 1987 and later, this amount increases to $600,000.

For more information, get Publication 448, "Federal Estate and Gift Taxes."

1991 INCOME TAX ITEMS OF INTEREST TO OLDER AMERICANS

Recent legislation made many changes to the tax law which affect the 1991 tax year. Some of the tax changes are as follows:

1. *Exemptions.*—The personal exemption increases to $2,150 for 1991.

2. *Standard deduction.*—For 1991, the standard deduction is $3,400 for single taxpayers; $2,850 for married filing separate taxpayers; $5,000 for head-of-household taxpayers; and $5,700 for qualifying widows and widowers, and married taxpayers.

If you are age 65 or older or blind in 1991, you are allowed an additional standard deduction amount depending on your filing status.

3. *Personal interest.*—For tax year 1991, no personal interest (such as interest on car loans or credit card balances) can be deducted as an itemized deduction.

4. *Filing requirements.*—The amount of gross income you may receive before you are required to file a tax return has increased and is shown below. The chart below does not apply if you can be claimed as a dependent or you are self-employed.

Filing status	*Gross income*
Single:	
Under age 65	$5,550
Age 65 or older	$6,400
Married Filing Joint Return:	
Both spouses under age 65	$10,000
One spouse age 65 or older	$10,650
Both spouses age 65 or older	$11,300
Not living with spouse at the end of year (or on date spouse died)	$2,150
Married Filing Separate Return	$2,150
Head of Household:	
Under age 65	$7,150
Age 65 or older	$8,000
Qualifying Widow(er):	
Under age 65	$7,850
Age 65 or older	$8,500

5. *Cosmetic surgery.*—Unnecessary cosmetic surgery will not be an allowable medical deduction. It will be an allowable medical deduction if the cosmetic surgery or procedure is necessary to improve a deformity arising from, or directly related to, a congenital abnormality, a personal injury resulting from an accident or trauma, or a disfiguring disease.

6. *Earned income credit.*—The earned income credit has been changed for 1991. There are three sections to the credit and the eligibility requirements have been modified. The maximum credit for each section is: (1) Basis Credit—for one child is $1,192 and for two children is $1,235; (2) Supplemental Young Child Credit is $357; and (3) Health Insurance Credit is $428.

7. *New Tax Rates.*—The income tax rates are now 15 percent and 28 percent, and 31 percent instead of 15 percent and 28 percent.

For more information on changes for tax year 1991 see Publication 553, "Highlights of 1990 Tax Changes."

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